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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION SEVEN

GUY VASILOVICH et al., Plaintiffs and Respondents, v. PATRICK BLANEY et al., Defendants and Appellants.	B170133 (Los Angeles County Super. Ct. No. PC021236)

APPEAL from an order of the Superior Court of Los Angeles County. L. Jeffrey Wiatt, Judge. Affirmed.

Glickman & Glickman and Steven C. Glickman for Defendants and Appellants.

Greenwald, Pauly, Foster & Miller, Andrew S. Pauly and Andrew J. Haley for Plaintiffs and Respondents.

The primary issue in this appeal is whether real estate sellers who made a statutory offer to compromise were entitled to recover their litigation costs and attorney fees. In this case it is undisputed the buyers could not achieve a more favorable judgment than the sellers' offer to compromise because the sellers filed for bankruptcy prior to trial on the merits of the buyers' damages and remedies. The trial court denied the sellers' motion for costs. We affirm.

FACTS AND PROCEEDINGS BELOW

Defendants and appellants, Patrick and Dianne Blaney, owned a residence in Northridge. Their home was severely damaged by the Northridge earthquake on January 17, 1994. The Blaneys decided not to make repairs but to build virtually an entirely new home instead.

The Blaneys were experienced in dealing in real estate. Dianne Blaney worked for decades as a real estate loan officer for various financial institutions. Patrick Blaney was a licensed broker and had worked in the real estate appraisal business since the early 1970's.

Most of the construction proceeded as planned. The Blaneys then contracted with American Home Improvement, Inc. to build a concrete tile roof, install windows and doors, install landscaping and an irrigation system and to perform other jobs. Near the end of the Blaneys' construction project American Home Improvement, Inc. abandoned work. The Blaneys were required to hire other work crews to finish the project as well as to perform remedial work to correct improperly installed windows and doors and the like.

The month the Blaneys moved into their new home it rained and the new roof, according to Dianne Blaney, "leaked like hell." The Blaneys hired a skilled craftsman to perform repairs on the roof. The Blaneys noticed no further roof leaks during the balance of the rainy season.

In May 1997 the Blaneys filed a complaint against American Home Improvement, Inc. with the State Contractors Licensing Board. Their complaint alleged poor

workmanship, abandonment and fraud. At the same time the Blaneys filed a claim against American Home Improvement, Inc.'s surety bond to recoup monies paid for work not completed, improperly completed or never done. Also in May 1997, the Blaneys filed a lawsuit against American Home Improvement, Inc., its principal and its employee for breach of contract, negligence and fraud. Their complaint sought damages of $100,000.

The Blaneys listed the home for sale in July 1997. Plaintiffs and respondents, Guy and Linda Vasilovich, made a purchase offer on the house. A licensed roofing contractor hired by the Blaneys made some minor repairs and informed the Blaneys he believed the roof was now "watertight." The home inspector hired by the Vasiloviches made a visual inspection of the roof and detected no apparent defects. The inspector similarly found no evidence of water damage when he inspected the attic.

On the transfer disclosure statement the Blaneys stated they were not "aware of any significant defects/malfunctions in" the roof. On the transfer disclosure statement the Blaneys also stated they were not aware of "[a]ny lawsuits by or against the seller threatening to or affecting real property including lawsuits alleging a defect or deficiency in this real property. . . ."

Less than two months after escrow closed the Vasiloviches discovered the roof had serious leaks. Water leaked into several rooms from the windows and from the recessed lightening. The house had to be entirely tarped over to prevent further interior damage. A later invasive inspection revealed numerous and serious flaws in the roof's construction.

The Vasiloviches brought suit against the Blaneys seeking damages of approximately $400,000. Their complaint alleged causes of action for, among other things, misrepresentation and failure to disclose. The Blaneys cross-complained for breach of contract based on the Vasiloviches' failure to make timely payments under the $60,000 second trust deed.

In July 1999 the Blaneys made a statutory offer to compromise for $15,000. The Vasiloviches rejected the offer.

The parties agreed to a bench trial before Judge Howard J. Schwab. The parties further agreed to bifurcate the issues of liability and damages. After a nine-day trial the court found for the Blaneys. The court concluded the Blaneys had not violated any duty to disclose the prior roof leaks.[1] Thereafter the Blaneys moved for an award of attorney fees and costs as the prevailing parties on the contract.[2] The court awarded the Blaneys only $1,000 of the more than $198,000 they sought in attorney fees. The court reasoned it would have been prudent for the Blaneys to disclose their prior history with the roof and thus concluded the lesser amount was appropriate in the circumstances.

The Vasiloviches appealed the court's ruling on liability and the Blaneys separately appealed from the court's award of fees and costs. We found substantial evidence supported the court's finding the Blaneys honestly believed problems with the roof had been corrected and thus had justifiably represented they were not aware of any defects with the roof. On the other hand, we found the Blaneys had violated their statutory duty to disclose their lawsuit against the construction company responsible for the roof.[3] Accordingly, we reversed the judgment in favor of the Blaneys and remanded with directions to conduct a trial of the unresolved issues of the Vasiloviches' damages and remedies. Because we reversed the judgment we found the Blaneys were no longer the prevailing parties and did not reach the issues raised in their cross-appeal.

After the remittitur issued from this court the Blaneys filed a voluntary chapter 7 bankruptcy petition. Further proceedings in the case were stayed by operation of law.[4] In September 2002 the Blaneys received a discharge in bankruptcy, including a discharge of their liability in this case.[5] The discharge prevented the Vasiloviches from proceeding

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[1] With the court's finding on liability, the Blaneys elected to dismiss their cross-complaint.

[2] Civil Code section 1717.

[3] *Vasilovich v. Blaney* (Feb. 27, 2002, B141819 [nonpub. opn.]).

[4] 11 United States Code section 362.

[5] 11 United States Code section 524.

with the action. They filed a request for dismissal without prejudice which the trial court ultimately ordered.

Thereafter, the Blaneys filed a memorandum of costs for almost $209,000, consisting primarily of attorney fees. The Blaneys argued they were entitled to an award of costs under Code of Civil Procedure section 998 because the Vasiloviches had not received a more favorable judgment than their statutory offer to compromise for $15,000. The Vasiloviches filed opposition, as well as a motion to strike or tax the Blaneys' request for fees and costs.

After extensive briefing and oral argument, Judge L. Jeffrey Wiatt denied the Blaneys' motion for costs and fees and granted the Vasiloviches' motion to tax those costs and fees. The court concluded it could not determine whether the Blaneys' statutory offer of compromise was reasonable because the Vasiloviches were prevented from obtaining a verdict on their claimed damages because of the Blaneys' discharge in bankruptcy. The court also found the Blaneys' discharge in bankruptcy left the Vasiloviches no choice but to dismiss the action. The court concluded it would frustrate the purpose of Code of Civil Procedure section 998 of encouraging settlements, and thus not serve the ends of justice, to permit the Blaneys to recover costs and fees in these circumstances.

The Blaneys appeal from the adverse ruling.

DISCUSSION

I. STANDARD OF REVIEW.

In construing Code of Civil Procedure section 998, we review the trial court's decision to deny the Blaneys' motion for an award of fees and costs de novo.[6]

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[6] *Berg v. Darden* (2004) 120 Cal.App.4th 721, 726 ["In a case such as this, involving the construction of a statute and its application to undisputed facts, our review

"With respect to the validity, or reasonableness, of a section 998 offer, we review the trial court's determination for an abuse of discretion. [Citation.]"[7] "'In interpreting section 998, [courts have] placed squarely on the offering party the burden of demonstrating that the offer is a valid one under section 998. [Citation.] The corollary to this rule is that a section 998 offer must be strictly construed in favor of the party sought to be subjected to its operation.' *(Barella v. Exchange Bank* [(2000)] 84 Cal.App.4th [793] at p. 799.)"[8]

We review the issues raised in this appeal with these standards in mind.

II. THE BLANEYS' VOLUNTARY BANKRUPTCY PREVENTED TRIAL OF THE VASILOVICHES' DAMAGES WHICH IN TURN PREVENTED PROOF THE STATUTORY OFFER EXCEEDED A POTENTIAL VERDICT; ACCORDINGLY THE BLANEYS CANNOT DEMONSTRATE ENTITLEMENT TO COSTS UNDER CODE OF CIVIL PROCEDURE SECTION 998.

Code of Civil Procedure section 998 states any party to an action "may serve an offer in writing upon any other party to the action to allow judgment to be taken . . . in accordance with the terms and conditions stated at that time."[9] However, "[i]f an offer made by a defendant is not accepted and the plaintiff fails to obtain a more favorable

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is de novo."]; *Burch v. Children's Hospital of Orange County Thrift Stores, Inc*. (2003) 109 Cal.App.4th 537, 543 ["The facts relevant to Burch's appeal are undisputed. Therefore, we review de novo the trial court's denial of Burch's motion for an award of prejudgment interest and expert witness costs."]; *Bihun v. AT&T Information Systems, Inc*. (1993) 13 Cal.App.4th 976, 999 ["In the present case the relevant facts are undisputed. . . . Thus, the case raises a pure question of law involving the interpretation and applicability of Civil Code section 3291 and Code of Civil Procedure section 998."].

[7] *Mesa Forest Products, Inc. v. St. Paul Mercury Ins. Co*. (1999) 73 Cal.App.4th 324, 329.

[8] *Burch v. Children's Hospital of Orange County Thrift Stores, Inc., supra*, 109 Cal.App.4th 537, 543.

[9] Code of Civil Procedure section 998, subdivision (b). All further statutory references are to the Code of Civil Procedure unless otherwise noted.

judgment . . . , the plaintiff shall not recover his or her postoffer costs and shall pay the defendant's costs from the time of the offer."[10]

"Section 998 is intended 'to encourage settlement by providing a strong financial disincentive to a party—whether it be a plaintiff or a defendant—who fails to achieve a better result than that party could have achieved by accepting his or her opponent's settlement offer. (This is the stick. The carrot is that by awarding costs to the putative settler the statute provides a financial incentive to make reasonable settlement offers.)'"[11] "Simply put, section 998 'penalizes [an offeree] who fails to accept what, in retrospect, is seen to have been a reasonable offer.' (*Harvard Investment Co. v. Gap Stores, Inc*. (1984) 156 Cal.App.3d 704, 713.)"[12]

The Blaneys point out the Vasiloviches received nothing in this litigation and thus their statutory offer to settle for $15,000 was necessarily more than what the Vasiloviches received. The Blaneys accordingly claim the trial court erred as a matter of law in failing to grant their motion under section 998 for an award of costs, including contractual attorney fees.

Nothing in the language of the statute nor in any case interpreting it supports their argument. We note the Blaneys cite no decision in support of their position. This is because the Blaneys' interpretation of section 998 is not, and cannot be, the law.

Nor can their proposed result be defended on logical grounds. It would be absurd to interpret the statute to permit the Blaneys to use their bankruptcy to thwart the Vasiloviches' ability to obtain a money judgment and then point to their lack of a money judgment as the basis of their right to claim costs and fees under section 998. Such an interpretation of section 998 would be contrary to the statute's policy of encouraging settlement because it would create an incentive to make only unreasonably low offers. If

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[10] Section 998, subdivision (c)(1).

[11] *Berg v. Darden, supra*, 120 Cal.App.4th 721, 726-727, quoting *Bank of San Pedro v. Superior Court* (1992) 3 Cal.4th 797, 804.

[12] *Mesa Forest Products, Inc. v. St. Paul Mercury Ins. Co., supra*, 73 Cal.App.4th 324, 330.

an offeror could manipulate the outcome of the litigation to ensure the offeree is never permitted to secure a judgment more favorable than a section 998 offer, then offerors could and would make unreasonable offers with impunity.[13] It would also create unwarranted windfalls to offerors if they could, by their own actions, control the litigation in such a way as to prevent the offeree from securing a more favorable judgment yet make themselves eligible for costs. Such a result is not in keeping with the goal of the statute of encouraging settlement by providing an incentive to make reasonable settlement offers.

As the Vasiloviches point out, to permit the result the Blaneys seek would be analogous to permitting a party who prevented another party's performance on a contract to then sue for breach of contract. Such a result is not permitted in contract law and we will not interpret the statute to permit what would be an equally absurd result under section 998.[14] Instead, we adopt "the construction that comports most closely with the apparent intent of the Legislature, with a view to promoting rather than defeating the general purpose of the statute, and avoid an interpretation that would lead to absurd consequences. . . . The legislative purpose will not be sacrificed to a literal construction of any part of the statute."[15]

The Blaneys claim the Vasiloviches' refusal to accept their statutory offer to settle "forced" them into bankruptcy. They assert bankruptcy is "simply one of the 'vagaries of litigation' for which the party rejecting a reasonable settlement offer must bear the risk."

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[13] See, e.g., *Pineda v. Los Angeles Turf Club, Inc*. (1980) 112 Cal.App.3d 53, 62-63 [affirming denial of expert witness fees under section 998 because prevailing defendant's pretrial offer was unreasonably low in light of its enormous liability exposure, presenting no reasonable possibility of acceptance and little risk to the defendant].

[14] See, e.g., Civil Code section 1511 [preventing performance of a contract may excuse performance and thus does not constitute a breach]; *Wilson v. Wal-Mart Stores, Inc*. (1999) 72 Cal.App.4th 382, 389 [because the process of settlement and compromise "is a contractual one, it is appropriate for contract law principles to govern the offer and acceptance process under section 998[]" provided such principles 'neither conflict with the statute nor defeat its purpose', . . . "].

Their argument finds no support in the record as a factual matter. The Blaneys timed their bankruptcy filing—not to the Vasiloviches' refusal of their settlement offer—but to this court's conclusion three years later the Blaneys were liable to the Vasiloviches for having violated their statutory duty to disclose pending litigation negatively affecting the property.

Although inapposite, the Blaneys rely on the decision in *Saakyan v. Modern Auto, Inc*. in support of their argument bankruptcy is simply one of the "vagaries of litigation" for which the Vasiloviches must bear the risk.[16] In *Saakyan*, the plaintiffs in a personal injury action made statutory offers to compromise. The defendant rejected the offers. The first trial ended in a special verdict for the defendant. Thereafter the trial court granted the plaintiffs' motion for new trial based on prejudicial juror misconduct. After the second trial a jury returned a special verdict in favor of the plaintiffs and awarded substantial damages which far exceeded their statutory offers to compromise. The plaintiffs moved for prejudgment interest and expert witness fees under section 998. The defendant opposed the motion for prejudgment interest and moved to tax costs. The trial court granted the defendant's motion, reasoning the plaintiffs' offers were extinguished by the verdict for the defendant in the first trial.[17]

The appellate court reversed. The court held a statutory offer to compromise under section 998 is not extinguished by a judgment vacated by a subsequent order for new trial.[18] The court also rejected the defendant's alternative arguments. "We reject defendant's argument that our holding functions as a disincentive to settlement and undermines the policy behind these statutes. To the contrary, the vagaries of litigation, undermines the policy behind these statutes. To the contrary, the vagaries of litigation, including the possibility of juror misconduct or reversal on appeal, which increases the

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[15] *Mesa Forest Products, Inc. v. St. Paul Mercury Ins. Co., supra*, 73 Cal.App.4th 324, 330, internal citations and quotation marks omitted.

[16] *Saakyan v. Modern Auto, Inc*. (2002) 103 Cal.App.4th 383.

[17] *Saakyan v. Modern Auto, Inc., supra*, 103 Cal.App.4th 383, 388-389.

[18] *Saakyan v. Modern Auto, Inc., supra*, 103 Cal.App.4th 383, 386.

opposing party's costs, are part of the risk inherent in rejecting a section 998 offer. . . . Defendant should not be allowed to take advantage of juror misconduct (which misconduct neither plaintiffs nor defendant caused) to avoid the consequences of the risk it took, by rejecting the statutory offers to compromise and forcing the matter to trial. . . . "[19]

The *Saakyan* decision does not assist the Blaneys. It does not stand for the proposition the offering party's bankruptcy is an inherent risk of litigation for which the party rejecting a statutory settlement offer must bear the risk. Moreover, in *Saakyan*, neither party was responsible for triggering the new trial which resulted in a more favorable judgment for the plaintiffs. In this case, by contrast, the Blaneys were responsible for preventing the Vasiloviches from obtaining a better result by voluntarily filing for bankruptcy, and by timing their bankruptcy filing to coincide with this court's remand order directing a trial of the Vasiloviches' damages. The Blaneys' bankruptcy foreclosed the possibility of a trial of the Vasiloviches' damages and for this reason they had no choice but to dismiss the action. Thus, and also unlike the situation in *Saakyan*, there was no money judgment to compare to the statutory offer to determine whether the Vasiloviches had achieved a more favorable judgment.[20]

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[19] *Saakyan v. Modern Auto, Inc., supra*, 103 Cal.App.4th 383, 391-392.

[20] The Blaneys correctly argue section 998 does not expressly require a judgment on the merits in order to determine whether a judgment was "more favorable." The statute only speaks of a "more favorable judgment" and does not specifically require a "judgment on the merits" in order to determine whether a statutory offer to compromise was more favorable than the ultimate "judgment." The Blaneys also correctly observe a dismissal with prejudice can qualify as a "judgment" for entitlement to costs under section 998. (See section 581d [written orders of dismissal constitute judgments for all purposes]; *Winick Corporation v. Safeco Ins. Co. of America* (1986) 187 Cal.App.3d 1502 [the defendant who was dismissed from the action because of the plaintiff's failure to serve and return summons within three years received all the relief it hoped to achieve; thus as a practical matter the defendant qualified as the prevailing party and was entitled to an award of attorney fees].)

However as noted, "[t]he legislative purpose will not be sacrificed to a literal construction of any part of the statute." (*Mesa Forest Products, Inc. v. St. Paul Mercury Ins. Co., supra*, 73 Cal.App.4th 324, 330.) Given the circumstances of the forced

It would be unfair to award the Blaneys fees and costs under section 998 when the Blaneys' bankruptcy, and not the merits of the Vasiloviches' case, nor any act or omission on the Vasiloviches' part, was the only reason the Vasiloviches could not achieve a more favorable judgment. It would also create an unwarranted windfall for the Blaneys whose bankruptcy discharge made the Vasiloviches powerless to prove their damages exceeded the statutory offer.

We thus hold because the Blaneys' bankruptcy discharge prevented trial of the Vasiloviches' damages and the opportunity to obtain a better result than the Blaneys' statutory offer, the Blaneys are precluded from claiming costs and fees under section 998.[21] We therefore further conclude the trial court did not err in denying the Blaneys' request for fees and costs under section 998.

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dismissal in the case at bar, it cannot be deemed the "judgment" for purposes of comparing its result with the Blaneys' statutory offer. Through no fault of their own the discharge of the Blaneys' liability in bankruptcy prevented the Vasiloviches from proving their damages exceeded the Blaneys' statutory offer. Because of the bankruptcy discharge they had no choice but to dismiss the action. The court ultimately ordered the action dismissed, but did so *without* prejudice.

This is not a case where the party's own dereliction caused the dismissal. (Compare, *Winick Corporation v. Safeco Ins. Co. of America, supra,* 187 Cal.App.3d 1502.) Nor is this a case where the Vasiloviches voluntarily dismissed their action because they realized it had no merit. To the contrary. In our prior opinion this court found the Blaneys were liable to the Vasiloviches for having violated their statutory duty to disclose the pending lawsuit alleging defects in the property. In other words, there would have been a judgment on the merits, and there would have been a money judgment to compare to the statutory offer to compromise, had the Blaneys' discharge in bankruptcy not precluded trial of the Vasiloviches' damages.

[21] In light of our conclusion, it is immaterial whether the trial court erred in finding the Blaneys' statutory offer was unreasonable and/or whether the trial court erred in placing the burden on the Blaneys to show the reasonableness of their offer. Accordingly, we need not and do not reach these issues. We similarly need not reach the issue whether the trial court erred in finding the Blaneys' motion for costs was timely filed.

DISPOSITION

The order is affirmed. Respondents are awarded their costs of appeal.

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JOHNSON, J.

We concur:

PERLUSS, P.J.

ZELON, J.